

THE INFLUENCE OF CEO EX-AUDITOR BACKGROUND, CEO EXPERT POWER, AND CEO OWNERSHIP POWER ON FINANCIAL STATEMENT READABILITY

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ABSTRACT

This study examines the influence of three CEO characteristics—prior experience as an auditor (Ex-Auditor), expert power, and ownership power—on the readability of financial statements in the banking sector in Indonesia. The sample includes 42 banks listed on the Indonesia Stock Exchange (IDX), observed over four years from 2020 to 2023, resulting in 168 firm-year observations. Purposive sampling was used to select firms that disclosed relevant CEO information and published financial statements in English. Readability was assessed using the Gunning Fog Index, which was explicitly applied to the narrative disclosures in the notes and financial statements. Results from multiple linear regression analysis show that CEO Ex-Auditor experience and CEO Expert Power significantly and positively affect financial statement readability. In contrast, CEO Ownership Power does not exhibit a vital influence. These findings underscore the role of experience-based leadership in enhancing the clarity and transparency of corporate financial disclosures.

Keywords: CEO Ex-Auditor, CEO Expert Power, CEO Ownership Power, Readability.

INTRODUCTION

In an era of increasing demands for corporate transparency and accountability, the readability of financial statements has become a critical factor in enabling stakeholders to comprehend, evaluate, and act upon company information. Among the various components of financial reports, the notes to the financial statements—referred to in Indonesia as Catatan atas Laporan Keuangan (CALK)—contain narrative disclosures that provide detailed explanations of financial figures, accounting policies, and non-financial information such as legal contingencies or corporate events. Due to their length and complexity, the readability of these notes often determines how effectively financial information is communicated to investors, regulators, and other stakeholders.

While the format of primary financial statements (such as income statements and balance sheets) is largely standardized by accounting standards, CALK offers companies a degree of flexibility in language, structure, and disclosure style. Consequently, the clarity and accessibility of these notes are influenced not only by regulatory requirements but also by internal managerial decisions—including those made or approved by the Chief Executive Officer (CEO). As the top executive with authority to approve financial disclosures, the CEO plays a central role in determining how information is presented to the public.

Several studies have highlighted how top executives' backgrounds, expertise, and incentives can shape financial reporting outcomes. For instance, Seifzadeh et al. (2020) found that CEO characteristics influence financial statement readability in Iranian firms. Mustapha et al. (2020) showed mixed results in Nigerian companies, with CEO ownership power being significant but

CEO tenure showing no effect. In Indonesia, research by Rizky (2019) and Sumayyah et al. (2020) examined the impact of CEO tenure and ownership on financial reporting quality but did not directly investigate narrative readability. These prior studies often focused on general disclosure quality, earnings management, or audit quality, leaving a gap in understanding how specific CEO characteristics influence the readability of disclosures—particularly in the context of CALK. Moreover, few studies have examined the influence of CEOs who were formerly auditors (CEO Ex-Auditor) on the presentation of financial narratives, even though such individuals may possess specialized knowledge in structuring transparent and audit-friendly reports. Similarly, CEO expert power, typically reflected by tenure, and ownership power, reflected by shareholding, may influence disclosure practices. However, their combined effect on the readability of financial statements, especially within a regulated and capital-intensive industry like banking in Indonesia, remains underexplored. This study seeks to fill that gap by analyzing the relationship between CEO Ex-Auditor status, expert power, and ownership power on the readability of financial statements in Indonesian banking firms over the 2020–2023 period. By focusing on the Gunning Fog Index applied to English-language financial disclosures, this research provides empirical insights into how CEO backgrounds affect the clarity and comprehensibility of corporate financial reporting.

LITERATURE REVIEW

This study is anchored in Upper Echelon Theory, which posits that organizational outcomes—strategic decisions, structures, and performance—reflect top executives' values, experiences, and cognitive bases (Hambrick & Mason, 1984). Rather than treating the firm as a rational, impersonal entity, the theory argues that key decision-makers shape the direction and character of the firm based on their characteristics. In financial reporting, Upper Echelon Theory suggests that how transparent, accessible, or complex a firm's disclosure is may depend on the CEO's background, expertise, and power dynamics. As the person responsible for approving and overseeing financial disclosures, the CEO's attributes are likely to be mirrored in financial statements' style, tone, and readability.

While past studies have linked CEO traits to various aspects of financial reporting quality, very few have explicitly focused on readability, particularly in the context of CALK in Indonesian banking firms. Most existing literature has examined either CEO power in general (Ting et al., 2017) or the effects of audit backgrounds on earnings management (Albrecht et al., 2018), but not their influence on how information is linguistically presented and comprehended by users. This study contributes to the literature by simultaneously analyzing three distinct CEO characteristics—Ex-Auditor status, Expert Power, and Ownership Power—and their impact on the narrative readability of financial statements using a Fog Index approach. By doing so, it highlights how leadership background and control dynamics can shape the accessibility of financial communication.

A CEO with previous experience as an auditor may possess greater sensitivity to the information needs of users and a deeper understanding of audit standards, regulatory expectations, and reporting clarity. Executives who previously worked as auditors will likely have heightened awareness of accounting standards, regulatory expectations, and the importance of clarity in disclosures. According to Upper Echelon Theory, this experience shapes how these individuals process information and make decisions—including how they instruct their teams to communicate financial information. Auditor-trained CEOs may push for clearer, more standardized disclosures. Albrecht et al. (2018) suggest that accounting

competence among executives can improve or worsen reporting outcomes depending on the incentives involved. Seifzadeh et al. (2020) found that CEO characteristics influence readability, though auditor background was rarely studied.

Hypothesis H1: CEOs with prior auditing experience positively influence the readability of financial statements.

Expert power refers to the accumulated knowledge and credibility a CEO gains through long-term experience. CEOs with longer tenures may have a firmer grasp of internal processes and external communication needs. According to the Upper Echelon Theory (Hambrick & Mason, 1984), executive decisions reflect their values and experiences. Therefore, a tenured CEO may be more capable of shaping transparent disclosures to align with stakeholder expectations.

Ting et al. (2017) associate tenure with CEO influence in disclosure quality, while Mustapha et al. (2020) found no significant relationship with financial reporting quality in Nigeria. The results remain inconclusive.

Hypothesis H2: CEO Expert Power positively influences the readability of financial statements.

Ownership power refers to the CEO's dual role as manager and part-owner of the firm. While Agency Theory emphasizes incentive alignment, Upper Echelon Theory interprets ownership as a psychological and positional attribute that may reinforce the CEO's influence on strategic outcomes. A CEO who owns shares may be more motivated to present disclosures that appeal to investors; however, the extent to which this motivation translates into improved readability depends on the individual's communication style and priorities. Mustapha et al. (2020) found a positive effect of CEO ownership on financial reporting quality, but its impact on readability remains unclear. Some research suggests that ownership may prioritize internal control over external communication.

Hypothesis H3: CEO Ownership Power positively influences the readability of financial statements.

RESEARCH METHODE

This study adopts a quantitative approach with a causal-explanatory design to examine the relationship between CEO characteristics and the readability of financial statements. The research investigates whether a CEO's background as a former auditor, tenure in office (expert power) and ownership of company shares (ownership power) influence the linguistic clarity of financial disclosures, particularly in the banking sector in Indonesia.

The population of this study includes all banking companies listed on the Indonesia Stock Exchange (IDX). A purposive sampling technique was employed to select companies that meet the following criteria: (1) the company is listed in the IDX, (2) the company publishes annual reports and financial statements in English consistently over the period 2020 to 2023, and (3) the company discloses sufficient data regarding the CEO's background, tenure, and ownership status. Based on these criteria, 42 banking firms were selected, yielding 168 firm-year observations across four years.

This study uses secondary data obtained from publicly available sources. Annual reports and audited financial statements were downloaded from the official IDX website (www.idx.co.id) and company websites. CEO background information, tenure data, and shareholding status were extracted from the reports' corporate governance and management profile sections.

Table 1. Variabel dan measurement

Variables	Proxy	Measurement	Data Source
Financial Statement Readability (FSR)	Fog Index	0.4 [(words / sentences) + percent of complex words]	English Version of Financial Statement
CEO Ex-Auditor (CEOEX)	Auditor experience	Years of experience as an auditor	Annual Report (Directors Profile)
CEO Expert Power (CEOTEN)	CEO Tenure	Total number of months the individual has served as CEO up to the end of the reporting period	Annual Report (Directors Profile)
CEO Ownership Power (CEOOWN)	CEO Ownership	binary variable coded one if the CEO owns company shares and zero if not	Annual Report (Directors Profile) and Financial statement notes

The study employs multiple linear regression analysis with the following model specification:

$$FSR = \alpha + \beta_1 CEOEX + \beta_2 CEOTEN + \beta_3 CEOOWN + e$$

RESULT AND DISCUSSION

This study analyzes 168 firm-year observations from 42 banking firms listed on the Indonesia Stock Exchange from 2020 to 2023. The main objective is to examine whether CEO characteristics—specifically prior auditing experience, expert power reflected by tenure, and ownership power—affect the readability of financial statements, as measured by the Gunning Fog Index applied to the English version of the notes to the financial statements.

Table 2. Statistics Descriptive Result

For Ratio Scale					
Variables	N	Minimum	Maximum	Mean	Standard Deviation
CEOEX	168	0	5	1.756	0.8113
CEOTEN	168	12	130	32.543	15.657
FSR	168	13.5	29.8	16.675	1.897
For Nominal Scale					
CEO OWN	168	0 =47%		1 = 53%	

Descriptive analysis reveals substantial variation across firms regarding CEO background and the linguistic clarity of their disclosures. Most of the firms had CEOs without auditing backgrounds, with tenure lengths and ownership status varying significantly. The Fog Index scores suggest a moderate level of readability on average, though some firms displayed considerably higher complexity in their narrative disclosures.

Table 3. Regression Result

Variables	Coefficient	Sig	Result
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Cons	32.238		
CEOEX	2.252	0.004	H1 Supported
CEOTEN	2.007	0.031	H2 Supported
FSR	1.071	0.207	H3 Not Supported
Adjusted R ²	15.6%		

$$FSR = 32.238 + 2.252 \text{ CEOEX} + 2.007 \text{ CEOTEN} + 1.071 \text{ CEOOWN}$$

The results indicate that CEO Ex-Auditor and CEO Expert Power have a statistically significant and positive effect on the readability of financial statements. In contrast, the regression results show that CEO Ownership Power does not substantially impact financial statement readability.

The regression results reveal that CEO Ex-Auditor experience significantly positively affects financial statement readability ($\beta = 2.252$, $p = 0.004$), supporting Hypothesis 1. This finding aligns with the Upper Echelon Theory of Hambrick and Mason (1984), which posits that executives' professional backgrounds shape their strategic decisions. CEOs with auditing experience appear to transfer their specialized knowledge and professional standards to financial reporting practices, resulting in more accessible disclosures. This result is consistent with Albrecht et al. (2018), who suggested that accounting competence among executives can influence reporting outcomes, though they focused primarily on earnings management rather than readability. Our findings extend their work by demonstrating that auditing experience contributes explicitly to more transparent communication. Similarly, Seifzadeh et al. (2020) found that CEO characteristics influence financial statement readability in Iranian firms, and our study confirms this relationship specifically for ex-auditor status in the Indonesian banking context. The positive influence of auditor experience on readability can be attributed to several mechanisms. First, former auditors are trained to identify unclear or ambiguous information that could mislead financial statement users. Second, they possess specialized knowledge of regulatory expectations and best practices in disclosure. Third, having evaluated numerous financial statements as auditors, they likely developed an appreciation for clarity and transparency that influences their approach when approving corporate disclosures.

Our analysis shows that CEO Expert Power, measured by tenure, positively influences financial statement readability ($\beta = 2.007$, $p = 0.031$), supporting Hypothesis 2. This finding suggests that as CEOs accumulate experience within their organizations, they develop more significant influence over reporting processes and a deeper understanding of effective communication strategies. This result partially contrasts Mustapha et al. (2020), who found no significant relationship between CEO tenure and financial reporting quality in Nigerian companies. However, it aligns with the theoretical framework proposed by Ting et al. (2017), who associated longer tenure with increased CEO influence over disclosure decisions. Our finding suggests that experienced CEOs leverage their accumulated knowledge in the Indonesian banking sector to enhance the clarity of financial narratives. Several factors may explain the positive effect of CEO tenure on readability. Long-serving CEOs likely develop stronger relationships with financial reporting staff, allowing them to influence the reporting process better. Additionally, experienced CEOs may have gained a clearer understanding of stakeholder information needs through repeated interactions with investors, analysts, and regulators, prompting them to prioritize communication clarity. Moreover, tenure provides the

authority and confidence to emphasize understandability over technical complexity in reporting.

Contrary to Hypothesis 3, CEO Ownership Power does not significantly affect financial statement readability ($\beta = 1.071$, $p = 0.207$). This finding challenges the assumption that alignment of ownership interests automatically leads to improved disclosure quality regarding linguistic accessibility. This result diverges from Mustapha et al. (2020), who found a positive effect of CEO ownership on financial reporting quality in Nigerian firms. However, their study focused on broader reporting quality metrics rather than specifically on readability. Our finding suggests that while ownership may motivate CEOs to ensure accurate reporting (as proposed by Agency Theory), it does not necessarily incentivize them to prioritize the clarity of narrative disclosures. Several interpretations could explain this non-significant relationship. First, the highly regulated nature of the banking sector may limit managerial discretion in disclosure practices, regardless of ownership incentives. Second, ownership may have contradictory effects on readability. While it aligns CEO interests with external stakeholders (encouraging transparency), it may also enhance managerial power to pursue personal communication preferences that are not necessarily aligned with readability. Finally, this study's dichotomous measurement of ownership may not have captured the nuanced effects of varying ownership levels.

From a theoretical perspective, our findings provide mixed support for Upper Echelon Theory in the context of financial disclosure readability. The significant results for CEO Ex-Auditor experience and Expert Power confirm that executive characteristics influence organizational outcomes, as proposed by Hambrick and Mason (1984). However, the non-significant result for Ownership Power suggests that not all aspects of executive power translate into disclosure strategies similarly. This study also contributes to Agency Theory discourse by highlighting that mechanisms designed to align principal-agent interests (such as CEO ownership) may not effectively address all dimensions of information asymmetry. While ownership may motivate accurate reporting, our results suggest it does not necessarily enhance the clarity of communication—an essential aspect of transparency.

Practically, our findings have several implications for corporate governance. First, they suggest that boards of directors in banking institutions should consider candidates' professional backgrounds, particularly auditing experience when selecting CEOs if they wish to enhance disclosure transparency. Second, the positive effect of tenure indicates that continuity in leadership may benefit reporting clarity, challenging the notion that regular CEO turnover is always optimal. Finally, reliance on ownership incentives alone appears insufficient to ensure readable disclosures, suggesting that governance mechanisms should specifically address communication quality. For regulators, these results imply that attention should be paid to the content of disclosures and their presentation and accessibility. Given that CEO characteristics significantly influence readability, regulatory frameworks might need to include more specific guidance on clarifying narrative disclosures to ensure consistent communication quality across firms with diverse leadership profiles. For investors and other financial statement users, our findings highlight the importance of considering management backgrounds when evaluating the quality of corporate disclosures. Financial statements from firms led by CEOs with auditing experience or longer tenure may provide more accessible information, potentially reducing the resources required to extract relevant data for decision-making.

Overall, this study demonstrates that financial statement readability in the Indonesian banking sector is significantly influenced by the CEO's professional background and experience, while ownership incentives play a less crucial role. These findings emphasize the need for a comprehensive approach to corporate governance that considers the multifaceted nature of executive influence on disclosure transparency.

CONCLUSION

This study investigates how CEO characteristics—specifically prior auditing experience, expert power through tenure, and ownership power—influence the readability of financial statements in the Indonesian banking sector. Grounded in Upper Echelon Theory, the findings affirm that top executives' cognitive backgrounds and experiences shape strategic outcomes, including how firms communicate financial information to external stakeholders.

The results show that CEOs with prior auditing experience and those with longer tenures are associated with more readable financial disclosures. These findings support the idea that decision-makers imprint their values, preferences, and communication styles onto the organization. In contrast, CEO ownership power does not significantly impact readability, suggesting that psychological engagement or cognitive framing—as reflected in experience and expertise—may play a stronger role than financial alignment. These insights hold practical implications for corporate governance, especially in leadership selection. Boards may benefit from prioritizing candidates whose backgrounds support clarity in communication, particularly in sectors where stakeholders rely heavily on financial disclosures for decision-making.

Future research could extend this work by incorporating additional psychological or demographic CEO attributes such as educational background, leadership style, or risk preference. Studies in different sectors or cross-country comparisons may also reveal contextual variations in how executive characteristics influence disclosure quality. Furthermore, integrating qualitative insights into CEOs' decision-making processes could offer a deeper understanding of how leadership shapes what is reported and how it is reported.

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